

## INLAND REVENUE BOARD OF REVIEW DECISIONS

### Case No. D56/93

Profits tax – purchase of property for redevelopment – subsequent sale – whether surplus subject to profits tax.

Panel: T J Gregory (chairman), Norman Ngai Wai Yiu and Lincoln Yung Chu Kuen.

Date of hearing: 8 March 1993.

Date of decision: 8 February 1994

The taxpayer was a private company which acquired certain properties. The properties could not be redeveloped unless the adjacent buildings could also be acquired. The adjacent buildings were not acquired and the properties were resold at a substantial profit. The properties had been purchased in mid-1988 and were sold in February/March 1989. At the hearing witnesses were called to give evidences including the chairman of the board of the taxpayer who also owned the majority of its shares.

Held:

The taxpayer had not discharged the onus of proof placed upon it. The clear evidence was that the properties were not capable of redevelopment on their own and the purchase price was met from an interest bearing loan. The rental income was not sufficient to service the debt. Much of the evidences given by the principal witness was rejected by the Board.

**Appeal dismissed.**

Case referred to:

Simmons v Inland Revenue Commissioners 53 TC 461

D3/92, IRBRD, vol 7, 61

Chinachem Investment Co Ltd v CIR 2 HKTC 261

D11/80, IRBRD, vol 1, 374

Cunliffe v Goodman [1950] 2 KB 237

H Bale for the Commissioner of Inland Revenue.

Anthony L Brown of Messrs Price Waterhouse for the taxpayers.

Decision:

## INLAND REVENUE BOARD OF REVIEW DECISIONS

### 1. THE SUBJECT MATTER OF THE APPEAL

The Taxpayer appealed against the determination of the Commissioner ('the determination') issued on 17 November 1992 in which he upheld the assessment to profits tax of a gain from the sale of certain properties.

### 2. THE FACTS

The facts, which are not in dispute, may be summarised as follows:

- 2.1 The Taxpayer was incorporated as a private company in 1988 and at all material times its authorised and paid up capital was \$10,000.
- 2.2 In mid-1988 the Taxpayer acquired two adjacent buildings and a third adjacent building in Place X ('the properties'). The purchase price was \$9,300,000 and was financed by an interest bearing advance from an affiliated company but repayable on demand.
- 2.3 The Taxpayer obtained some assistance from an architect in assessing the viability of a redevelopment and obtained a rental feasibility study.
- 2.4 The results of investigations indicated that the site of those of the wholly owned properties was inadequate to justify a redevelopment but that a redevelopment would be viable if the remainder of the partly owned building and two other adjacent buildings could be acquired.
- 2.5 Attempts were made to negotiate the acquisition of the additional properties but for various reasons which are immaterial to this decision purchases could not be negotiated.
- 2.6 In late February 1989 and early March 1989 unsolicited offers were received from agents for the properties and by an agreement for sale and purchase dated early 1989 the properties were sold for \$18,500,000. The transaction was completed in April 1989.
- 2.7 The accounts of the Taxpayer from incorporation to 31 March 1989 classified the properties as a fixed asset. The accounts for the year ended 31 March 1990 showed a profit of \$8,690,085.88 on the sale of the properties but the Taxpayer's proposed tax computation did not offer that profit for assessment.
- 2.8 The assessor did not accept the Taxpayer's claim that it is intended to hold the properties as a long term investment after a redevelopment and on 29 January 1991 the assessor raised the following profits tax assessment on the Taxpayer.

## INLAND REVENUE BOARD OF REVIEW DECISIONS

Loss per Return	(\$72,579)
<u>Add</u> : Profit on sale of the Property	<u>8,690,086</u>
Assessable Profits	\$8,617,507
<u>Less</u> : Set-off of loss brought forward	<u>513,968</u>
Net Assessable Profits	<u>\$8,103,539</u>
Tax Payable thereon	<u>\$1,337,083</u>

2.9 The Taxpayer, through its tax representative ('the representative'), objected to the assessment and the matter was referred to the Commissioner for his determination which, as already stated, was issued on 17 November 1992 and upheld the assessment.

### 3. THE CASE FOR THE TAXPAYER

The Taxpayer was represented by a firm of certified public accountants ('the representative'). The representative in an opening submission argued that the Commissioner's determination was wrong and focused attention on certain aspects of the determination which it was submitted were incorrect.

### 4. THE EVIDENCE

The representative called three witnesses.

#### 4.1 The First Witness

4.1.1 In chief:

4.1.1.1 She was a widow and, at all material times, was the chairman of the board of directors of the Taxpayer. She was also the beneficial owner of the majority of its issued shares.

4.1.1.2 She stated that the properties were purchased for rental income. She described her relationship with one of her co-directors until his sudden and untimely death. She stated that she relied heavily on this individual's judgment and that he had considered it would be beneficial for the company to acquire the properties as the location was good. She also believed that his plan was to acquire the balance of the partly owned building and the two adjacent buildings. She appreciated that they might not succeed in buying these adjacent buildings but the decision was to endeavour so to do.

4.1.1.3 At the time the properties were purchased the decision was taken to hold them for rental income if the Taxpayer was successful in acquiring the adjacent properties. At the time of purchase the Taxpayer appreciated that the rental

## INLAND REVENUE BOARD OF REVIEW DECISIONS

income would be insufficient to cover the company's operating expenses for the first one to two years. As the Taxpayer could increase the rentals every two years and as its directors were confident of obtaining increases in rentals of 30% to 40% on each occasion rentals could be increased, the rental yield would exceed the outgoings. At the time of purchase rentals were low but with the prospect of rental increases the properties were a viable long term investment.

4.1.1.4 She was chairman of the group of companies of which the Taxpayer was a member ('the group') and she applied a lot of her time and effort for charitable purposes. She considered the purchase of good properties in good locations a good strategy. She explained how she met the now deceased co-director after her husband's death in 1973 and stated that she had total confidence in him and when he suggested the purchase of the properties she agreed. She stated that the group had sufficient funds available and referred to a credit facility with the Hong Kong branch of Bank A. She explained that her co-director had died in his sleep in February 1989 whilst still in his early 50s. She was shaken by his death and she was less confident without benefit of his advice.

4.1.1.5 She confirmed that a letter dated 1 March 1989 from a firm of solicitors was unsolicited but brokers would have known of the co-director's death. She stated that the Taxpayer had not advertised the properties for sale and stated that her co-director's early death was a sign of bad luck.

4.1.1.6 The proceeds of sale were paid to the Taxpayer's parent company which had purchased a property on Hong Kong Island where all the tenants were well established companies.

4.1.2 Cross-examination:

4.1.2.1 She confirmed that the Taxpayer learned of the properties from the deceased co-director but she made the decisions. Since his death she used large firms of real estate agents as advisors.

4.1.2.2 When she was told about the properties she had compared the purchase price with the rental income. The rental income was low but could be increased. She had not herself approached the architect but the deceased co-director had authority to negotiate all investments and only approached her for the final decision.

4.1.2.3 She was referred to a letter of 19 August 1991 from the architect to the Inland Revenue Department and stated that the architect did not know about the situation but supplied information as requested by the Revenue. She was unable to say whether the architect had been instructed to prepare sketch plans and a feasibility study and could not explain a paragraph in that letter. She was then referred to various drawings which were partly prepared by the architect but was unable to identify those as the documents referred to in the first

## INLAND REVENUE BOARD OF REVIEW DECISIONS

paragraph of the letter. Having been referred back to the architect's letter she stated that the properties were purchased for income as the site could not be developed on its own. The balance of the partly owned building and the two adjacent buildings were required for a redevelopment. She confirmed that the architect had been instructed to prepare a feasibility study as one was necessary to enable the Taxpayer to be aware of its options and to be able to decide which to adopt.

- 4.1.2.4 She was referred to an undated document headed 'Cash Flow/Management Budget' and a document, apparently dated '6/88', headed 'Rental Return Feasibility Study' and confirmed that they had been received by the Taxpayer from the architect. She had not had written advice from the architect but only verbal advice. When referred to the Cash Flow/Management Budget document she was only prepared to say that she thought she had seen it but was unable to say that it had been prepared after completion of the purchase of the properties. She was then taken through the document and eventually asked what the return on a redevelopment would have been. She stated that the question should be put to her accountant. She denied that she had selected one of the options and stated that it was not so urgent to opt one way or the other.
- 4.1.2.5 She was questioned extensively about the rental return study but was unable to give any satisfactory answers. She was unable to explain why one of the sites was apparently included in the proposal and stated that the deceased co-director's had not explained his ideas to her. She explained that a search of the late co-director's papers had been unable to identify any relevant papers.
- 4.1.2.6 She was asked to produce the Taxpayer's minute book which she did. She confirmed that the minute book was a loose leaf file and that there was only three original minutes. When asked whether there was only three meetings she replied that if there was a meeting there was a minute but if there was no minute it had only been a discussion. She was pressed as to whether there had been an actual meeting on 11 July 1988, a meeting at which the Board had resolved to acquire the properties. She replied, 'if there was a minute there was a meeting.'
- 4.1.2.7 She herself had played no part of her negotiation to purchase the properties. It had been dealt with by the deceased co-director who kept her informed over tea or lunch.
- 4.1.2.8 She was asked about an offer on the part of the Taxpayer to purchase one of the adjacent properties and answered that no reply had been received. A counter-offer of some 60% in excess of the original offer was rejected as it was too expensive.
- 4.1.2.9 She was asked if the budget had been exceeded and stated that there was no budget. She was asked why the counter-offer was rejected, bearing in mind that the price was reasonable, a statement which she denied.

## INLAND REVENUE BOARD OF REVIEW DECISIONS

- 4.1.2.10 She was then reminded that the Taxpayer purchased the properties for \$9,000,000 and sold them for \$18,500,000. Her reply was she had been lucky.
- 4.1.2.11 She claimed that she was a timid person. She had been happy to go ahead with the project until the death of her co-director. She was not inclined to go ahead after his death.
- 4.1.2.12 She described the site as a good site as it was in demand by hawkers. She was not aware whether plans had been prepared or there had any meetings with the Building Authority.
- 4.1.2.13 After it was decided to sell the properties brokers went to her office. Brokers searched registers and identified the owners and endeavoured to persuade owners to sell. She was then shown a letter dated 28 February 1989 from an individual offering to purchase the properties. She stated that this individual was a very good friend of hers but she would never sell to a good friend. She did not know whether he was connected with the ultimate buyer. She was then referred to the solicitors' letter of 1 March 1989 and confirmed that the firm of solicitors named in that letter were the Taxpayer's solicitors. She explained that a broker had come to see her but had been asked to go to a lawyer as she wanted a concrete offer as she did not know the broker. She had identified her solicitors to the broker. She was unable to identify which offer she eventually accepted but said that the offer was also unsolicited. She was then asked about the directors' meetings on 1 March 1989 and confirmed that there had been a meeting.
- 4.1.3 Questions from the Board:
- Having been briefly re-examined, in response to questions from the Board:
- 4.1.3.1 She stated that she had four children and, at the material times, all were studying abroad. One daughter had returned one month the hearing before to work for her.
- 4.1.3.2 She was also asked whether the deceased co-director had told her what his ideas were when he proposed the purchase of the properties. She said that he had told her that the properties were on offer at a reduced price and were fully occupied and attracted hawkers. If the Taxpayer acquired the adjacent properties a redevelopment could be considered. He had also told her that it was not easy to get adjacent owners to join in a redevelopment and that they needed to calculate a return on the investment. He had told her that a redevelopment would be a good investment as he was very keen on the location.

## INLAND REVENUE BOARD OF REVIEW DECISIONS

4.1.3.3 Her attention was drawn to the Taxpayer's accounts which showed a loss of \$640,000 as at 31 March 1989. She stated they were not concerned as the investment was a long term investment. It was pointed out that even with a 40% increase every second year it would take a considerable period of time for the Taxpayer to catch up with losses. She said that she regarded certain of the expenses as one-off expenses.

4.1.3.4 She was asked to what extent the facilities from Bank A had been drawn. She stated that the details were known to her accountant. Her programme was to buy a property each year and that the group had an annual retail income of some \$60,000,000.

### 4.2 The Second Witness

4.2.1 In chief:

4.2.1.1 He was a manager in the estate management division of the group of which the first witness was chairman. He had been with the group since 1982 and confirmed that the Taxpayer was a member of the group. He had assisted the deceased who was an executive manager.

4.2.1.2 He stated that the deceased co-director was very experienced in property matters having previously worked for a leading bank in Hong Kong. He also confirmed that the deceased co-director had considerable influence on the group's property investment policy which was to hold properties as assets for long term income.

4.2.1.3 He stated that the intention of the Taxpayer in buying the properties was to hold them as a long term investment and that the rental income from them was acceptable even if the Taxpayer was able to acquire the adjacent properties. The redevelopment of the properties would have been a considerably more ambitious project than any project previously undertaken by the group.

4.2.1.4 The Taxpayer had held the properties for some eight months and made a loss on the rentals. However, on the basis of a 30% increase after two years the loss would be reduced. He also believed that the group purchased other properties on the expectation that rental increases would eliminate initial losses.

4.2.1.5 The properties had not been advertised for sale. He was referred to the solicitors' letter and stated that he had not made a request for that letter to be written.

4.2.1.6 The proceeds of sale were invested in another property which was held in rental income which was far superior.

4.2.2 Cross-examination:

## INLAND REVENUE BOARD OF REVIEW DECISIONS

- 4.2.2.1 He stated that he and the deceased co-director had been the only estate management officers although he had an assistant. He reported to the deceased co-director.
- 4.2.2.2 He stated that the group policy was set by the chairman and was communicated to him by both the chairman and the deceased co-director.
- 4.2.2.3 He confirmed that the rental income from the properties was \$550,000 and that with a 30% increase in rentals after two years he considered that the investment would be profitable.
- 4.2.2.4 He confirmed that the properties were old buildings and subject to rent control.
- 4.2.2.5 He also stated that the property on Hong Kong Island had been purchased showing a loss.
- 4.2.2.6 He was referred to feasibility studies which he stated he had come across both before and after the purchase of the properties.
- 4.2.2.7 He had not been involved in any negotiations for purchase of the adjacent properties. His responsibility had been to send out letters on the instructions of the deceased co-director.
- 4.2.2.8 He had played no part in the negotiations for the sale of the properties.
- 4.2.3 Re-examination:
- He confirmed that the deceased co-director had not kept him informed as to what was going on.
- 4.2.4 Questions from the Board:
- 4.2.4.1 He stated that, to the best of his recollection, the deceased co-director had joined the group in 1985.
- 4.2.4.2 When he had first taken up that employment the group owned a commercial building and some individual ground floor shops and some rental units. Between 1982 and 1989 the only properties owned by the group which had been sold were the properties.
- 4.3 The Third Witness
- 4.3.1 In chief:



## INLAND REVENUE BOARD OF REVIEW DECISIONS

- 4.3.1.1 He was an executive manager of the group and had been with the group for four years.
- 4.3.1.2 He confirmed that he had prepared the Cash Flow/Management Budget and that it was based on discussions with the architect.
- 4.3.1.3 He had contacted the architect when an enquiry had been received from the Revenue as to cash flows and budgets etc. He confirmed that the architect had produced the documents without any difficulty.
- 4.3.1.4 He confirmed that the first witness, the chairman, was the group's policy maker.
- 4.3.1.5 He was then asked if he was aware of the 'Residual Method of Valuing Property'. He confirmed that he had discussed it with the architect. It had also been mentioned by the architect in meetings.
- 4.3.1.6 He confirmed that had the properties been retained without redevelopment rental increases of approximately 30% would be possible every second year. On the basis of a 30% increase every second year the rental income would cover the Taxpayer's borrowing expenses after four years and all expenses after five years. The main expense was interest.
- 4.3.1.7 He also confirmed that most of the proceeds from the sale of the properties was invested in the property on Hong Kong Island which was a better investment as it was a larger site, all the tenants were well-established companies with much of the rental guaranteed and the potential was much greater. He identified a schedule of tenants and the rents of this property which had been provided to the Taxpayer at the time of purchase.
- 4.3.1.8 He was then questioned further about the documents originating from the architect and about his approach to the architect to be able to reply to questions from the Inland Revenue. He said that the architect had told him that he had prepared the figures in 1988.
- 4.3.1.9 He confirmed that the percentage rate of return on the property on Hong Kong Island was a percentage of the purchase price.
- 4.3.1.10 He stated that the group had the resources to redevelop the properties and the adjacent properties had they been acquired.
- 4.3.2 Cross-examination:
- 4.3.2.1 He was a university graduate and had been with the group since April 1989.

## INLAND REVENUE BOARD OF REVIEW DECISIONS

4.3.2.2 He gave the purchase price of the property on Hong Kong Island and confirmed that a loss was still being made. He stated that most of the group's properties incurred a loss in the early years but that the potential could be identified.

4.3.3 Questions from the Board:

He confirmed that since 1990 the group had purchased and sold properties within a short period of time and that a company had been set up to do this. He had described this as a 'reorganisation'.

4.4 THE FIRST WITNESS

The first witness was then recalled and was reminded that she was still under oath.

4.4.1 In chief:

4.4.1.1 She was questioned about the earlier sale of a property. She explained that a company had sold its shares in a commercial building which had been owned for some forty years. The investment was a minority investment and was difficult to dispose of.

4.4.1.2 She also had sold a small school in Place W which had to be closed. This was in 1986. The school had been held for some twenty years. Another member of the group owned a much better school in Kowloon and had never traded in property.

4.4.1.3 The group had a company which had been set up in 1991 which purchased and sold properties. This particular company had been established as her children regarded her as too conservative and dealing in properties for short term gains was teaching her to become more aggressive. There had only been one or two transactions.

5. Question to both Representatives

After the witness had completed her evidence a member of the Board advised the representative of the Taxpayer and the representative for the Revenue that he was distantly related to the wife of a brother of the witness' late husband. He explained that he did not know either the witness nor her late husband. The Board asked if either party had any objection to the case continuing in light of that information but both the representatives stated that they had no objection.

6. Submission for the Taxpayer

The representative then made a concluding submission.

## INLAND REVENUE BOARD OF REVIEW DECISIONS

- 6.1 He stated that he had regarded it as unreasonable for the Commissioner to use the Taxpayer's compliance with the assessor's request for information, namely the 'cash flow management of this development project', as evidence of a dealing intention of the part of the Taxpayer particularly as they were supplied long after the properties had been acquired. The Board was referred in detail to the relevant correspondence.
- 6.2 The Board was also taken through the detail of the interest payments and advised that the potential was for the properties to be profitable whereby the Commissioner was not correct in supposing that it would have been necessary for the Taxpayer to sell the completed redevelopment.
- 6.3 Further criticisms of the determination of the Commissioner were made.
- 6.4 The Board was referred to Simmons v Inland Revenue Commissioners (Simmons Tax Cases 1980 page 350 and 53 TC 461) particularly the passage in the speech of Lord Wilberforce where he said:
- 'Frustration of a plan for investment, which compels realisation, even if foreseen as a possibility, surely cannot give rise to an intention to trade.'
- 6.5 A comparison between the facts of that case and this present appeal was then made and having referred to the often quoted passage from Lord Wilberforce's speech in the same case namely:
- 'What I think is not possible is for an asset to be both trading stock and permanent investment at the same time, nor for it to possess an indeterminate status, neither trading stock nor permanent asset.'
- 6.6 The representative stated that applying that to the properties the question was the status they possessed on the date of the purchase to mid-1988. It was submitted that there were several indications that they fell within the category of permanent investments; there are the directors' minutes dated mid-1988 stating that the properties were purchased as part of a plan to develop them with the two adjacent properties into a commercial building for long term investment, there had been figures prepared showing the gross actual return from the completed project and there was also the description of the properties in the accounts for the period from incorporation to 31 March 1989 as 'fixed assets'. It was also a fact that the properties were never advertised for sale and that when they were sold it was as a result of an unsolicited approach. It was submitted that those facts showed that the properties were purchased as an investment and they did not fall into the category of trading stock ab initio simply because redevelopment project of which they were to be part was frustrated by the Taxpayer's inability to purchase the two adjacent properties.
- 6.7 The Board was then referred to its decision in D3/92, IRBRD, vol 7, 61.

## INLAND REVENUE BOARD OF REVIEW DECISIONS

- 6.8 The role of the deceased co-director was then referred to and the fact that his unexpected and untimely death had removed a valuable source of expertise and caused great personal distress to the chairman. A development project which had taken off with high hopes in June and July 1988 ended in misfortune whereafter the properties represented unluckiness and unhappy memories so that when unsolicited offers were received the decision to sell was taken.
- 6.9 The Board was asked to find that the properties were purchased by the Taxpayer as a capital asset and were not transferred into trading stock prior to their unsolicited sale whereby the gain was a capital gain specifically excluded from the charge to profits tax under section 14 of the Ordinance.

### 7. SUBMISSION BY THE REVENUE

- 7.1 The submission of the Revenue was also in writing and the question for the Board was identified, namely whether the profit the Taxpayer derived from the disposal of the properties was chargeable to profits tax under section 14 of the Ordinance.
- 7.2 The attention of the Board was drawn to section 14 and section 2(1) and the definition 'trade'.
- 7.3 The Board was then referred to passages from the following cases:
- 7.3.1 Simmons v CIR 53 TC 461
- 7.3.2 Chinachem Investment Co Ltd v CIR 2 HKTC 261
- 7.3.3 D11/80, IRBRD, vol 1, 374
- 7.3.4 Cunliffe v Goodman [1950] 2 KB 237
- 7.4 The representative of the Revenue then reminded the Board of the timing of the purchase of the properties, their description and the detail with respect to the sale.
- 7.5 The Board was referred to the minutes of the meetings at which the decision to purchase and sell were taken, namely the minutes of the meeting of 11 July 1988 and 1 March 1989. The representative of the Revenue queried whether these meetings had actually taken place. The Board was also asked to treat these minutes as self-serving.
- 7.6 The Board was reminded as to the evidence as to the work done by the architect and comments were made as to the cash flow. The Board's attention was also drawn to the correspondence between the Taxpayer's tax representative and the

## INLAND REVENUE BOARD OF REVIEW DECISIONS

IRD with respect to the assessment and the correspondence with respect to the attempted purchase of the adjacent properties.

7.7 The representative of the Revenue queried how the brokers got to know that the properties were for sale.

7.8 In summary, the representative of the Revenue submitted that on the evidence the Taxpayer appeared to have had no definite intention to redevelop the site for long term rental income. In July 1988, the time the properties were purchased, the adjacent properties were not owned by it. How, therefore, could the Taxpayer have had a definite intention to redevelop the combined sites? It was submitted that the evidence pointed to the conclusion that the Taxpayer may have been in two minds in which case the profit was a trading profit.

7.9 The Board was asked to consider the short period of ownership, self-serving directors' minutes and the evidence before the Board that the death of the co-director was the most important factor leading to the sale, a factor which had not been mentioned prior to 2 March 1993. The Board was also asked to take into account the evidence that no attempt had been made to apply for an order for possession and that the properties were sold subject to existing tenancies. The Board was reminded that the architect was not called to explain what he had been asked to do or what he had done. It was submitted that the evidence with respect to the attempt to purchase the adjacent building was not complete and, further, in a rapidly rising property market it would be unrealistic to stick to the original budget; the evidence with respect to the purchase of part of the building was incomplete and the Board had not been given a reason for this purchase.

7.10 A person or company may hold both fixed assets and trading stock. The fact that a company or group of companies does not have a history of trading does not preclude it from trading.

7.11 The Board was asked to find that the Taxpayer undertook a transaction in the nature of trade. It was submitted that the Taxpayer had not discharged the onus of proof that the properties were purchased as long term investment whereby the appeal should be dismissed.

### 8. REASONS FOR THE DECISION

8.1 Section 68 (4) of the Ordinance places the onus of proof on the taxpayer.

8.2 The evidence of the chairman of the group was that at the material times she was the ultimate decision maker but relied exclusively on her then co-director. She had first come into contact with this gentleman as a consequence of the death of her husband in 1973 and she held his judgment in very high regard. She asked the Board to accept that she would accept his recommendation

## INLAND REVENUE BOARD OF REVIEW DECISIONS

almost without question and it would appear from her evidence that the location of the properties and their appeal to hawkers were factors mentioned by him and which she accepted without demur. She also added that he advised her that the properties were available at a reduced price.

- 8.3 The Board accepts the evidence that the two wholly owned properties were incapable of redevelopment on their own and that the purchase price was met from an interest bearing advance from another group company. It also accepts the evidence that the rental income at the time of purchase was inadequate to service the interest on this debt. Although there was evidence that periodic increases in the rentals would be sufficient to service the debt after four or five years, the Board is unable to accept that evidence. First, all of the witnesses, the chairman and two employees of the group, were basing that claim on the assertion that 30% or 40% increases in rents could be obtained every second year but no independent witness was called to corroborate their evidence. Secondly, the buildings were described as being some twenty years old and, inevitably, if the properties were to be held as a long term investment the Taxpayer would have had to spend money on essential repairs and maintenance from time to time. Such expenditure does not appear to have been taken into account by the witnesses but that expenditure could become necessary and would defer, initially, or adversely impact, subsequently, profitability. The foregoing are matters which are relevant when assessing the weight to be attached to the evidence that the properties would be a satisfactory investment even if they could not be combined with others in a redevelopment. When considered with the other evidence, particularly the chairman's evidence that her then co-director was really interested in the properties because of their redevelopment potential, the Board is unable to attach any weight to the evidence that the Taxpayer's fall-back position was to retain the properties in their then existing state as a long term investment. Additionally, there is no mention in the minute of the meeting of 11 July 1988 of the Taxpayer retaining the properties for rental income if acquisition of the adjacent properties could not be achieved.
- 8.4 The Board was not convinced by the evidence as to why the adjacent properties were not acquired. The property market was rising and it is a well-known fact that the price to be paid for a property which is a key to a redevelopment is impacted by the owner's awareness of any such proposal. An uninvited offer for a building arouses its owner's curiosity as to the reason for the offer being forthcoming. Accordingly, the Board would have expected the evidence to be that the Taxpayer anticipated having to pay a higher price to secure the additional properties. As it is, however, the evidence as to the reason why the offer of the adjacent property was rejected lacks credibility.
- 8.5 The Taxpayer's chairman endeavoured to persuade the Board that she lacks expertise in the real estate market. However, her evidence was that the group is now in receipt of rental income totalling some \$60,000,000 per annum. She

## INLAND REVENUE BOARD OF REVIEW DECISIONS

endeavoured to persuade the Board that until his death she had been totally relied on her co-director and that she had concentrated on her charitable work. The Board is entirely satisfied that she is an extremely competent businesswoman and is unable to accept that she did not have a greater involvement in the decisions with respect to the properties than she would wish the Board to accept.

- 8.6 The representative of the Taxpayer asked the Board to accept that the properties were purchased with the intention to redevelop but that intention was frustrated by the Taxpayer's inability to acquire the outstanding parts of the partly owned building and the two adjacent buildings. The Board does not think that this situation parallels the situation which gave rise to Simmons v CIR upon which he relied. In that case legislation was introduced which made the economic climate unfavourable and frustrated the intention. In the present case the acquisition of the additional properties or the agreement of the owners to join with the Taxpayer was a known prerequisite to any redevelopment. The Board notes that neither of these options had been explored with those owners at the time of purchase. Even if the Board were to accept that a redevelopment was the ultimate goal, on the evidence at the time of acquisition a redevelopment was no more than a pipe dream, something very different to an intention.
- 8.7 The Board is satisfied that the Chairman well knew at the time the decision to purchase was taken that no risk was being run in acquiring the properties as the price being asked was, as already noted, a reduced price whereby they would be readily marketable if a redevelopment could not be undertaken because of the Taxpayer's inability to purchase the balance of the partly owned building and two adjacent buildings or secure the participation of their owners in the scheme.
- 8.8 The Board is obliged to treat the minutes of the directors' meeting of 11 July 1988 with considerable caution. In so saying the Board is conscious of the fact that the minute book is a loose leaf file.
- 8.9 The Taxpayer has failed to discharge the onus imposed on it by the Ordinance, namely to satisfy the Board that the properties were acquired as a capital asset and either in an as is state or as part of a redevelopment involving other properties.

### 9. DECISION

For the reasons given this appeal fails.